Global Market Outlook 2021

Navigating the new reality

Fidelity Australian Equities Fund

Paul Taylor

Finding structural growth opportunities in a crisis

When we look back to this period in five years' time, we will view it as an excellent time to have invested in the market, despite the uncertainty and volatility we may see over the near term.

What is your investment outlook for Australian equities in 2021? To what extent is this tied to virus-related developments?

We firmly believe that when we look back to this period in five years' time, we will view it as an excellent time to have invested in the market, while significant uncertainty is likely to continue in the short term and will likely cause some ongoing volatility. We have maintained this view that Fidelity's substantial research network, technological support and extensive investment experience will help us pick structural growth-led winners at attractive valuations, as we have during this turbulent year.

Australia and the world are simultaneously undertaking monetary and fiscal policy expansion. This is a very significant tail wind for the global economy and once we enter a post-COVID-19 recovery phase, it will likely be incredibly expansionary for global growth and a positive for Australian and global equity markets alike. Even if interest rates initially rise on the back of this expansionary phase, equity markets tend to perform well in the early phases of interest rate rises. That said, interest rate rises are still probably a year or two away, as we navigate the demand destruction resulting from COVID-19 measures. While we expect fiscal policy expansion to continue for many years to come, we believe it will change from helicopter money towards significant infrastructure development.

What do you think could surprise the market in 2021 (either positively or negatively)?

Some of the best scientific minds in the world have been focusing on developing a vaccine for COVID-19 and we have seen the upbeat response to recent news about high levels of efficacy of some vaccines under development. It would indeed be quite positive for both economic activity as well as investor sentiment, if such a vaccine would come to market sooner than expected and signs of a 90 per cent efficacy rate is, indeed, a step in this direction. It would facilitate economic activity, aid the resumption of travel and most importantly, restore the health and quality of human lives.

One of the extraordinary actions we've seen during the pandemic, has been governments' economic responses to the pandemic as they have manoeuvred quickly to safeguard economies. In Australia, the crisis broke our close to 30-year run of uninterrupted economic growth and in the second half of the year, we sank into recession. To maintain employment and survive shut-down restrictions, the Government has significantly increased its spending on unemployment and employment programmes. This has happened in different forms right around the world. Given the crucial role that stimulus support has played, any premature retraction of such support would be a negative surprise.

What themes, sectors or regions would offer opportunities or potential risks in a post COVID-19 world?

While the pandemic has caused considerable distress to human life, we have some observations from how day-to-day life has responded to this crisis. An interesting point to note, is that many of the key trends pre-COVID-19 have accelerated throughout the crisis and are well positioned to continue their structural growth in a post-vaccine world. These include:

- E-commerce
- Digital delivery of food and beverage

- Work from home
- Nesting
- Infrastructure
- Cashless society
- Active wear versus formal wear

While the world will recover from COVID-19, it's likely to be a different place and these trends will continue to shape the future. The strategy is driven by this long-term perspective, and thus is investing in good quality businesses benefiting from these themes and run by strong management teams. We have also been looking for fundamentally strong opportunities in pandemic-affected businesses. It is extremely important to distinguish between long-term winners that can create value for investors versus beneficiaries of positive news flow. Thus, we continue to assess the durability and strength of the underlying balance sheets and the long-term structural growth of the business, as well as the quality of the management teams to drive positive outcomes.

Given the extent of innovation we have witnessed this year, there are businesses that are falling behind on this front and have seen a structural pressure on their demand prospects.

Within your portfolio, what areas have highest convictions and what areas are you avoiding?

Crises often throw up opportunities to invest in long-term structural growth companies at attractive valuations. At the start of a crisis, equity markets 'shot first and asked questions later' and we converted this indiscriminate sell-off into an opportunity to buy into high-quality, long-term businesses that we believe will pay off over the next decade.

The portfolio is invested in large-cap, highly liquid blue-chip stocks. We remain mindful of company fundamentals and focus on the experience and competence of management teams, which is crucial to their ability to manage through the current uncertainty. Australia remains home to innovative companies that are well positioned to deliver long-term growth. We favour high-quality companies with a sustainable competitive edge, strong free cash flow generation and robust earnings growth.

At the same time, we maintain a cautious stance towards Australian banks overall. Their business is experiencing competition from technology-driven innovation, and banks that fail to keep pace will see erosion in business.

How do you expect sustainability factors to influence returns and how is this reflected in your portfolios?

In light of our long-term experience with investing, engaging with management teams, witnessing the development of business models, we do believe that good companies create value holistically. These companies are mindful of their impact beyond financials – their business models are mindful of the impact on society and the environment. Within Australia, we expect the spotlight will be on corporate governance issues as well as on remuneration issues in 2021. The Fidelity Australian Equities portfolio has always tilted towards high quality businesses that have been driven by proactive managements and the returns generated for our investors testify the soundness of this approach.